**Monetary policy in time of climate crisis (by Alain Lipietz)**

**Introduction**

After the US mortgage crisis that started in 2007-2008 and the euro crisis in 2010, the public became increasingly aware of two ecological crises: the energy-climate crisis and the food-health crisis. While the last one could be tamed by policy measures, the energy crisis requires more: huge investments. If humankind wants to escape a +2° increase in global heat by the 2030’s, it has to change its model of consumption and production *now*, with a maximum of greenhouse gas in 2020.[[1]](#footnote-1)

This later commitment is the challenge for the next elections to the European Parliament and for the Green movement, the more conscious political force regarding both social impacts of crises and the decisive threshold of the energy-climate crisis.

A mere monetary and credit policy would be insufficient. In the 1930s, the real divide introduced by Roosevelt's New Deal was a better direct sharing-out of value-added in favor of wages, a much bigger federal budget and the creation of a Welfare State. It should be the same in a “sustainable Europe”. You can provide lots of liquidity for your economy, but nothing will happen if effective demand is not increasing! And the emergency of the energetic transition (to cope with climate and nuclear hazards) requires an economy where new credits are funneled into proper investments, by contrast to the European policy-mix of the last ten years. Yet in what follows we focus on the monetary and credit aspects.

**Restrictive rules around the euro**

The legal targets for the American Federal Reserve system are twofold, with a democratic accountability to the Congress: price stability and growth of employment. By contrast, the euro was introduced with the mission for the European Central Bank (ECB) to first of all fight inflation, without regard for employment. Moreover, the ECB should not finance governments directly. That was aimed at appeasing the German public opinion, traumatized by hyper-inflation in the 1920’s. In order to fight inflation, the growth of the volume of money had to be limited. And the targeted inflation rate was zero, without an employment goal. The first ECB president, Wim Duisenberg, stuck to those rules. The next president, Jean-Claude Trichet, at first followed the same policy, to “anchor the credibility of the euro”. Until the crisis …

**A Policy for the New World**

From 1999 to 2009, I reported several times for the Economic and Monetary Comity of the European Parliament on ECB and European Investment Bank (EIB), and on the directive “Prudential rules and supervision of financial conglomerates”. Discussing with Trichet and the president of EIB, Philippe Maystadt, I was impressed by their deeper and deeper comprehension of the problems.

Trichet moved at first by giving up the control of the volume of money. Instead, the ECB concentrated on the control of interest rates. Moreover, he fixed the target of the inflation rate to “close to but below 2%”, thus acknowledging the benefits of some inflation which should make the economy work more smoothly. Facing the 2008 financial crash, he drastically lowered interest rates and engaged in “Quantitative Easing”. Quantitative Easing came down to the ECB buying massively government debt paper. This was a relieve to private banks that possessed a lot of government debt paper. These public debts, themselves, had outburst in 2008 when governments had to bail out private banks and firms facing the consequences of the mortgage crisis: a nationalization of private debts added to the previous public debts, mostly from Southern European governments. As a consequence, debt paper owned by private banks now came into the hands of the ECB and hence was 'europeanized'. This received a lot of opposition by orthodox economists, e.g. in the German Bundesbank. This was, nonetheless, a useful step as it prevented a new banking crisis.

Monetary Easing, however, was pure monetary policy. It hardly increased effective demand in the economy and it did not direct credits to an urgent Green Deal. This was the reason why the Green Party in the European Parliament demanded an alternative policy: massive Quantitative Easing and 0 % rates of interest should be restricted to the loans of EIB, given that the EIB is the only bank democratically accountable. Its money should be principally reoriented to the financing of the ecological transition. M. Meystadt agreed to the idea, yet nothing happened during the next years. Mario Draghi continued and intensified Trichet’s policy: indiscriminate low interest rates and Quantitative Easing, not regarding the purpose of this creation of credit-money.

The Green proposition remains the basis for a monetary policy in times of climate emergency. Recently, the economist Pierre Larrouturou and the IPCC member Jean Jouzel developed similar ideas in a “Finance-Climate Call” aiming at diminishing the Greenhouse gas emissions by a factor 4[[2]](#footnote-2).

**Clearing the old world**

The failure in directing finance to a new, sustainable world, is due to the weight of the past: the rescue of banks and the transfer of important amounts of private debt to the (public) Central Banks and then to ECB through Quantitative Easing after 2008. It could better be acknowledged that a substantial part of these debts will never be paid back. Alas, debates and decisions were concentrating on “How to pay for the debts”, with unbearable consequences for ordinary people, especially in the Greek case, and delays for ecological transition. And, despite some reforms (e.g. creation of the European Stability Mechanism), even big banks may appear weak in the case of a new future credit crisis as they are creditors to “weak” countries. The problem is beyond “sharing the risks”: Europe should solve the problem by a coordinated cancellation and rescheduling of debts.

The real problem in offsetting or rescheduling old debts is the risk of bankruptcy of creditors (like Cyprus banks, as a result of a partial cancellation of Greek debts). There exist solutions, such as the monetization of these “frost” credits in the case a creditor bank is in difficulties. In fact, the main problem is political: a part of the European opinion wants to “punish” indebted “lazy” countries. This is not a priority : climate is THE priority.

1. See <http://lipietz.net/Fears-and-Hopes-The-Crisis-of-the-Liberal-Productivist-Model-and-its-Green-2669> [↑](#footnote-ref-1)
2. <https://www.pacte-climat.eu/en/the-call/> [↑](#footnote-ref-2)